

Message Text

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C O N F I D E N T I A L SECTION 01 OF 03 LONDON 19565

E.O. WQQYTWC GDS

TAGS: PGOV, PINT, EGEN, PFOR, UK, EFIN

SUBJECT: BRITAIN IN NOVEMBER

REF: LONDON 17786

SUMMARY. IF OCTOBER WAS A BLEAK MONTH FOR BRITAIN -- AND IT WAS -- NOVEMBER PROVED EVEN MORE DESOLATE FROM THE GOVERNMENT'S STANDPOINT. ALTHOUGH THE POUND STRENGTHENED SLIGHTLY, OTHER ECONOMIC INDICATORS WERE AMBIGUOUS AND THE CONTENTIOUS 1975/76 PARLIAMENT DREW TO A BITTER CLOSE, THE GOVERNMENT'S PROBLEMS SEEMED TO MULTIPLY. NEGOTIATIONS WITH THE IMF DRAGGED ON, APPARENTLY DIVIDING THE CABINET AS WELL AS LABOR'S BACKBENCHERS. AND ADDING NEW STRESS TO THE GOVERNMENT'S TIES WITH THE TUC. IF THESE PROBLEMS WERE NOT ENOUGH, THE GOVERNMENT SAW ITS WORKING MAJORITY IN COMMONS CUT TO THE VANISHING POINT BY THE LOSS OF TWO SEATS IN BY-ELECTIONS; ITS PLANS TO NATIONALIZE THE AILING SHIPBUILDING AND AIRCRAFT INDUSTRIES STYMIED BY AN ASSERTIVE HOUSE OF LORDS; AND THE MILITANT MINERS UNION THREATENING A NATIONAL STRIKE. EUPHORIC FROM THEIR STRONG BY-ELECTION SHOWING AND SCENTING POLITICAL BLOOD -- PREMATURELY IN OUR VIEW -- THE CONSERVATIVES STEPPED UP THEIR ATTACK ON SEVERAL FRONTS, DRAGGING OUT THE HOARY "REDS UNDER THE BED" ALLEGATIONS. MRS. THATCHER JUGGLED HER SHADOW CABINET, SEEKING TO PRODUCE A MORE DYNAMIC, CREDIBLE FRONTBENCH, AND IN THE PROCESS MOVED ITS CENTER OF POLITICAL GRAVITY SEVERAL NOTCHES TO THE RIGHT. THE OPENING OF A NEW PARLIAMENT BROUGHT A TEMPORARY RESPITE FOR THE GOVERNMENT, BUT THE CENTRAL QUESTION OF HOW TO DEAL WITH THE CURRENT ECONOMIC CRISIS REMAINED UNANSWERED. END SUMMARY.

1. STERLING ACTUALLY ROSE BY 4.1 PERCENT AGAINST THE DOLLAR DURING NOVEMBER, AS MARKETS CALMED IN ANTICIPATION OF AN AGREEMENT ON CONDITIONS FOR BRITAIN'S \$3.9 BILLION IMF LOAN APPLICATION. THE IMF TEAM WAS GENERALLY EXPECT-
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ED TO RECOMMEND TOUGH CONDITIONS, BUT NEGOTIATIONS CONTINUED FOR TWO WEEKS LONGER THAN INTENDED, AGREEMENT PROVING FAR MORE DIFFICULT THAN EXPECTED.

2. MEANWHILE, THE ECONOMY CONTINUED TO EMIT CONFUSING SIGNS. INFLATION WAS MOVING UP TOWARD 15 PERCENT, WHILE INDUSTRIAL PRODUCTION AND MANUFACTURING INVESTMENT SHOWED WEAK INDICATIONS OF RECOVERY. NOTHING CAN BE SAID ABOUT

UNEMPLOYMENT SINCE THE STATISTICIANS WHO PRODUCE THAT INFORMATION WERE ON STRIKE. MONEY SUPPLY (M3) FIGURES FOR OCTOBER INDICATED THAT GROWTH WAS GREATER THAN HAD BEEN EXPECTED AFTER INCREASED SPECIAL DEPOSIT REQUIREMENTS, HIGHER INTEREST RATES AND THE SUBSEQUENT SALES OF GOVERNMENT DEBT. AS A RESULT, HMG REIMPOSED THE "CORSET" -- A DEVICE TO LIMIT THE EXPANSION OF DEPOSITS - ON THE BANKING SYSTEM, HOPEFULLY MAKING IT JUST POSSIBLE TO KEEP WITHIN THE M3 GROWTH TARGET RANGE OF 12 PER CENT FOR THIS FISCAL YEAR. THE RESULT WILL BE A SEVERE SQUEEZE ON LENDING TO THE PRIVATE SECTOR. HOWEVER, HMG HOPES TO EASE THIS PRESSURE BY BARRING STERLING LENDING BY BANKS TO FINANCE THIRD COUNTRY TRADE. THIS MEASURE IS A FURTHER NAIL IN STERLING'S COFFIN AS A WORLD TRADE CURRENCY, BUT IS EXPECTED TO RESULT IN THE RETURN OF 500 MILLION POUNDS FROM ABROAD.

3. AND WHAT TO DO ABOUT THE ECTNOMY? WITH THE HMG/IMF NEGOTIATIONS RUNNING LONGER THAN EXPECTED, THE GOVERN-

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MENT'S ECONOMIC PACKAGE IS STILL UNCERTAIN. PRESS AND EMBASSY SOURCES, HOWEVER, HAVE REPORTED THAT A CABINET POSITION IS BEGINNING TO TAKE SHAPE, AND THAT A STRONG MAJORITY OPPOSES DEFLATIONARY MEASURES POPULARLY ASSOCIATED WITH THE IMF MISSION. IF POPULAR ASSUMPTIONS ARE CORRECT, THE CABINET, ALONG WITH SUCH DISPARATE GROUPS AS THE CBI, THE TUC, THE NEO-KEYNESIANS AND LABOR BACKBENCHERS ON BOTH SIDES OF THE IDEOLOGICAL WATERSHED, WOULD BE AT ODDS WITH THE POSITION ATTRIBUTED TO THE IMF AND CHANCELLOR HEALEY. CALLAGHAN, BY ALL ACCOUNTS, IS STILL KEEPING HIS OPTIONS OPEN, BUT SOME BELIEVE HE HAS IMPLICITLY TILTED AWAY FROM THE TREASURY AND THE IMF. THIS INFERENCE IS DRAWN FROM CALCULATED LEAKS, THE PM'S UNUSUAL HANDLING OF THE ISSUE (THE CABINET WAS ASKED TO JUDGE THE CHANCELLOR'S PROPOSED ECONOMIC MEASURES, RATHER THAN TO ENDORSE MEASURES PREVIOUSLY AGREED UPON BY THE PM, THE CHANCELLOR AND A FEW KEY MINISTERS), AND FROM HIS HIGHLY TOUTED POLITICAL SENSITIVITY (EVEN DISREGARDING THE REPORTED CAINBET MAJORITY, THE VIEWS OF THE TUC AND LABOR BACKBENCHERS ARE ASSUMED TO CARRY CONSIDERABLE POLITICAL WEIGHT WITH HIM). SPECULATION ASIDE, BRITAIN'S

CREDITORS AND FX MARKETS MUST WAIT AWHILE LONGER FOR THE SOLUTION TO THIS ECONOMIC CONUNDRUM.

4. THE LOSS OF TWO TRADITIONALLY SAFE LABOR SEATS -- WALSALL NORTH AND WORKINGTON -- IN EARLY NOVEMBER BY-ELECTIONS WAS A SERIOUS PSYCHOLOGICAL AND PARLIAMENTARY BLOW TO THE GOVERNMENT. THE RESULTS CONFIRMED OPINION POLLS SHOWING VOTER SENTIMENT HAD SHIFTED SHARPLY IN THE CONSERVATIVES FAVOR, DEEPENING FRUSTRATION, DESPAIR AND BACKBITING IN THE LABOR CAMP. THE PARLIAMENTARY BALANCE WAS ALTERED, AS LABOR'S WORKING MAJORITY DROPPED TO A SINGLE SEAT. MOREOVER, FOUR MORE BY-ELECTIONS LIE AHEAD, TWO OF THEM INVOLVING "SAFE" LABOR SEATS. THE HOUSE OF LORDS ADDED TO THE GOVERN-
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MENT'S DISCOMFORT. BY-ELECTION RESULTS SEEMED TO REINFORCE THE PEERS' IDEOLOGICAL AND TACTICAL OPPOSITION TO CONTROVERSIAL BILLS, AS THEY EMASCULATED THE DOCK WORK REGULATION BILL (DUE TO ABSTENTIONS BY TWO RIGHT-WING LABOR MPS) AND STOPPED, AT LEAST TEMPORARILY, THE SHIPBUILDING AND AIRCRAFT NATIONALIZATION PROPOSAL. THE LORDS WERE ABLE TO FRUSTRATE THE GOVERNMENT, SECURE IN THE KNOWLEDGE THAT DEVOLUTION AND OTHER HIGH PRIORITY LEGISLATION WOULD PREVENT ANY REFORM OF THE ANACHRONISTIC UPPER HOUSE IN THE NEW PARLIAMENT. FROM THE GOVERNMENT'S STANDPOINT, THE END OF THE 1975/76 PARLIAMENT WAS TOO LONG ACOMING.

5. ANOTHER DISTURBING ELEMENT IN THE ECONOMIC AND POLITICAL PICTURES WAS THE DISPUTE BETWEEN THE MINERS AND THE NATIONAL COAL BOARD (NCB) OVER EARLY RETIREMENT. RELATIVELY WORSE OFF THAN MINERS IN OTHER WESTERN EUROPEAN COUNTRIES, THEY BELIEVE THEY HAVE A GOOD CASE FOR LOWERING RETIREMENT AGE 5 YEARS, TO AGE 60. THIS DEMAND, IF MET, WOULD BREACH THE PAY POLICY, AND IS OPPOSED BY THE GOVERNMENT AND THE TUC, AS WELL AS THE NCB. THE ISSUE HAS BEEN SUBMITTED TO A STRIKE VOTE, BUT UNION LEADERS AND NCB OFFICIALS BELIEVE A COMPROMISE SOLUTION WILL BE FOUND.

6. HAVING BLOODED THE GOVERNMENT IN THE BY-ELECTIONS, THE CONSERVATIVES PURSUED THEIR PREY VIGOROUSLY.

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ALTHOUGH IT IS STILL DIFFICULT TO ENVISAGE A SCENARIO THAT WOULD PRODUCE AN EARLY GENERAL ELECTION, THE TORY LEADERSHIP PRESSED ITS ADVANTAGE PUBLICLY AS WELL AS IN PARLIAMENT. ATTACKS ON THE GOVERNMENT'S FAILURE TO MOVE DECISIVELY ON THE ECONOMIC FRONT, TO ELIMINATE WELFARE ABUSES AND TO AMEND ITS PROGRAM GOALS IN THE LIGHT OF THE BY-ELECTION RESULTS WERE STEPPED UP. THE CONSERVATIVES ALSO RENEWED THEIR HOARY ALLEGATIONS THAT THE LABOR PARTY IS PENETRATED BY LEFT-WING SUBVERSIVES, THOUGH ONE TORY MP - IAN SPROAT -- APPEARS TO HAVE GONE TOO FAR AND FOUND HIMSELF FACING CHARGES OF BREACHING PARLIAMENTARY PRIVILEGE AND OF LIBEL.

7. WARMING TO THE CHASE AND APPARENTLY ANTICIPATING A QUICK, CLEAN KILL, CONSERVATIVE LEADER THATCHER MOVED TO STRENGTHEN HER SHADOW CABINET. FOREIGN AFFAIRS SPOKESMAN REGINALD MAUDLING, A LEADING MODERATE, WAS THE MAIN CASUALTY. WHILE THE CHANGES APPEAR TO HAVE STRENGTHENED THE TORY FRONTBENCH, THEY ALSO REPRESENTED A RIGHTWARD SHIFT IN PARTY LEADERSHIP.

8. THE QUEEN'S SPEECH OUTLINING THE GOVERNMENT'S LEGISLATIVE PROGRAM FOR THE 1976/77 PARLIAMENT CONTAINED NO SURPRISES -- DEVOLUTION WILL DOMINATE THE SESSION, ACCOUNTING FOR NEARLY TWO-THIRDS OF THE AVAILABLE TIME AND ENSURE THAT TEMPERGROW SHORT. AT THE CONCLUSION OF DEBATE ON THE SPEECH, THE GOVERNMENT TURNED BACK A TORY MOTION OF NO CONFIDENCE IN ITS ECONOMIC POLICIES BY A COMFORTABLE 10 VOTE MARGIN.

9. AT GENEVA, THE RHODESIA CONFERENCE FAILED TO MEET EARLY EXPECTATIONS, BOGGING DOWN ON THE DATE FOR INDEPENDENCE. WHILE THE DATE ISSUE IS OF LITTLE REAL CONSEQUENCE, IT BECAME A TEST OF POLITICAL MANHOOD FOR THE VARIOUS DELEGATIONS AND A BAROMETER OF BRITISH GOVERNMENT ATTITUDES. AS IT BECAME APPARENT THAT ONLY BRITAIN COULD BREAK THE DEADLOCK, CABINET SENTIMENT

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SHIFTED FROM AN ALMOST REFLEXIVE REFUSAL TO RE-ENTER THE RHODESIAN THICKET TO A GRUDGING WILLINGNESS TO PLAY A LIMITED ROLE. THE DIMENSIONS OF ITS ULTIMATE ROLE ARE STILL BEING DEFINED, BUT NOVEMBER INDICATED THAT HMG WILL NOT ABDICATE ITS RESPONSIBILITIES IN SOUTHERN AFRICA.

10. NOVEMBER ALSO SAW EC PRESIDENT-DESIGNATE ROY JENKINS ROUNDING OUT THE BRITISH TEAM, ACCENTING YOUTH, VIGOR AND COMMITMENT. HE DESIGNATED LABOR MP DAVID MARQUAND, REPUTEDLY THE MOST ABLE MAN ON THE BACK-BENCHES, AS HIS PRINCIPAL ADVISER, AND INFLUENCED THE SELECTION OF TORY MP CHRISTOPHER TUGENDHAT, A PROMISING YOUNG MODERATE, AS THE OTHER EC COMMISSIONER. ALTHOUGH THE GOVERNMENT ANNOUNCED IT WOULD SHORTLY INTRODUCE LEGISLATION FOR DIRECT ELECTIONS TO THE EUROPEAN PARLIAMENT, THERE IS CONSIDERABLE DOUBT WHETHER THE BILL CAN BE PASSED IN TIME TO MEET THE JULY 1978 TARGET DATE. CALLAGHAN'S POSTURE AT THE NOVEMBER 29-30 EUROPEAN COUNCIL MEETING REFLECTED HIS PRE-OCCUPATION WITH THE DOMESTIC ECONOMIC SITUATION: HE REJECTED DEVALUATION OF THE GREEN POUND, ENJOINED SURPLUS COUNTRIES TO ACCEPT SPECIAL RESPONSIBILITY FOR ECONOMIC RECOVERY AND OPPOSED STRICT CONDITIONS ON IMF BORROWINGS. WE ALSO UNDERSTAND HE PURSUED THE STERLING "SAFETY NET" SCHEME PRIVATELY.

11. SUMMARIZING, ECONOMIC UNCERTAINTY ONCE AGAIN DOMINATED EVENTS IN BRITAIN. THE IMF VISIT AND SPECULATION AS TO THE CONDITIONS TO BE IMPOSED ON THE BORROWING OVERSHADOWED ALL OTHER QUESTIONS IN THE MEDIA AND IN POLITICAL FORA, DOMESTIC AND INTERNATIONAL. CONCERN OVER THE ECONOMY PERMEATED ALL LEVELS AND WAS MOST STARKLY ETCHED IN THE BY-ELECTION RESULTS WHICH ADDED TO THE GOVERNMENT'S PROBLEMS. AGREEMENT ON THE TERMS OF THE IMF DRAWING WILL NOT ELIMINATE BRITAIN'S ECONOMIC PROBLEMS, BUT IT SHOULD RELIEVE THE TENSION, ALLOWING THE GOVERNMENT TO ACT AND TO FOCUS AT LEAST PART OF ITS ATTENTION ON OTHER PROBLEMS. ONE DOESN'T HAVE TO BELIEVE IN SANTA CLAUSE TO EXPECT SOME IMPROVEMENT, IF ONLY TRANSITORY, IN DECEMBER.

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